

Indiana Department of State Revenue

Revenue Ruling #2005-13ST

November 10, 2005

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ISSUE #1

Sales/Use Tax – Parent's acquisition of tools and subsequent sale of same to subsidiary

Authority: IC 6-2.5-5-8

The taxpayers request the Department to rule on the application of sales/use tax to the acquisition of tools and subsequent sale of same by the parent to the subsidiary.

ISSUE #2

Sales/Use Tax – Subsidiary's purchase of tools from parent

Authority: IC 6-2.5-5-8, IC 6-2.5-3-2

The taxpayers request the Department to rule on the application of sales/use tax to the purchase of tools from the parent by the subsidiary.

STATEMENT OF FACTS

Beginning on July 1, 2002, Distributor, headquartered in Indiana, entered into an agreement with its parent company, Supplier, also headquartered in Indiana, to distribute (sell) Supplier products throughout the United States. Effective July 1, 2003, Distributor and Supplier executed a new revised distribution agreement. Hereinafter, the distribution agreement between Distributor and Supplier in effect beginning July 1, 2002, through June 30, 2003, is referred to as the "First Agreement," and the revised distribution agreement between the Distributor and Supplier effective July 1, 2003, through the present date is referred to as the "Second Agreement." Under both the First Agreement and the Second Agreement, in addition to buying products from Supplier for resale, Distributor also purchased from Supplier certain tools that are required to correctly install or adjust the products.

Supplier purchases approximately 75% of the tools from third-party suppliers located both inside and outside of Indiana. These tools are delivered to Supplier in Indiana, where Supplier inspects

the tools and holds them in inventory. The remaining tools (approximately 25%) are machined by a subsidiary of Supplier also located in Indiana, that provides industrial processing services to Supplier in connection with those tools not acquired from third-party vendors. Supplier procures, owns and causes to be delivered to subsidiary all materials used to machine the tools by subsidiary. When completed, these tools are delivered by subsidiary to Supplier and inspected and held in inventory by Supplier, along with those tools acquired from third party suppliers. When Distributor informs Supplier that it wishes to purchase one or more tools, the tools are removed from inventory and they are then etched by Supplier to include the logo, trademark, work order, part number, size, diameter, and a tool code. After etching, the tools are then packaged, and delivered to Supplier's warehouse in Indiana, from which location they are shipped.

When Distributor purchases the tools from Supplier, in lieu of formal invoicing, the tools are charged to Distributor at Supplier's cost, removed from inventory on Supplier's books and records, and capitalized on Distributor's books and records, at cost.

While Distributor sells the products to its customers, Distributor only sometimes sells the tools for an extra charge. In most cases, Distributor supplies such tools to its customers at no extra charge. Distributor also makes available to its independent sales representatives a limited number of tools at no charge, for use by Distributor customers. Distributor continues to hold title to the tools supplied to its customers and sales representatives which must be returned to Distributor upon its request. However, after the Tools have been supplied to a hospital or medical care facility where they are used in patient care, they are only on rare occasions returned to Distributor.

Under the First Agreement, upon receipt of an order, Supplier would arrange for the shipment and delivery of the requisite products and tools from its inventory located in Indiana directly to Distributor's customer or sales representative by common carrier, and Distributor would pay and reimburse Supplier for all freight costs. Pursuant to the terms of the First Agreement, title and risk of loss to the products and tools passed from Supplier to Distributor either upon the delivery of those items to Distributor's customer if the delivery destination was inside the State of Indiana or at the Indiana state line if the delivery destination was outside the State of Indiana.

The First Agreement provided in part as follows:

Section 2.6 Delivery. Supplier shall cause delivery of the Products to the locations identified by Distributor in each purchase order. Title and risk of loss to the Products shall pass from Supplier to Distributor (i) upon delivery to Distributor's customer, if the delivery destination is inside the State of Indiana, and (ii) at the Indiana state line, if the delivery destination is outside the State of Indiana. Distributor shall pay and reimburse Supplier for all freight costs and each party shall bear its own insurance costs associated with the shipment and delivery of the Products. Supplier reserves the right to split an order and make delivery in installments or partial shipments, and in such event, each installment or partial shipment shall be separately invoiced and paid for when due, without regard to subsequent deliveries.

Under the Second Agreement, upon receipt of an order, Supplier would remove the requisite Supplier-made products and tools from its inventory in its Indiana warehouse and then move them to the packaging area in that warehouse for shipment by common carrier to Distributor's customer's or sales representative's location. Although all of this activity takes place in the Supplier warehouse, under the Second Agreement, Supplier is deemed to have delivered the products and tools to Distributor upon physical delivery of those items to the packaging area in Supplier's Indiana warehouse. Risk of loss and title to these items pass from supplier to Distributor at this point under the Second Agreement. Distributor is responsible for final packaging and shipping the product and tools under the Second Agreement.

The Second Agreement provides in part as follows:

Section 2.6 Delivery; Risk of Loss.

(a) The terms of delivery of the ordered Products shall be EXW, [Indiana] (Incoterms 2000), except that in addition to being responsible for shipping the Products, Distributor also shall be responsible for packaging all Products at Supplier's warehouse prior to shipment. Supplier shall be deemed to have delivered all Products to Distributor upon delivery of the Products to the packaging area at Supplier's warehouse in [Indiana] ("Delivery"). Upon and after the Delivery of the Products, Distributor shall be solely responsible for packaging the Products and all aspects of the loading, handling and shipment of the Products to Distributor's desired destination, and all costs, liabilities and obligations related thereto. Without limiting the foregoing, Distributor shall be responsible for identifying and contracting with all carriers and insuring the Products after Delivery. Supplier reserves the right to split an order and make Delivery in installments, and in such event, each installment shall be separately invoiced and paid for when due, without regard to any subsequent Delivery of Products. Distributor shall use commercially reasonable efforts to cause the Products to be packaged and shipped within two (2) business days of the Products being delivered to the packaging area of Supplier's warehouse in [Indiana].

(b) Title and risk of loss to the Products shall pass from Supplier to Distributor at the time of Delivery of the Products.

(c) Supplier shall designate a secure holding area in its [Indiana] plant where Distributor may store, keep or locate Products for which Distributor has taken Delivery. Products in such holding area shall be segregated from products of Supplier and its other customers. Supplier shall use commercially reasonable efforts to maintain secure and environmentally consistent conditions for such holding area comparable to the conditions it maintains for its own products. Notwithstanding the foregoing, Distributor understands and acknowledges that Supplier shall not be liable for loss or damage of any kind to the Products after Delivery of the Products by Supplier.

DISCUSSION – ISSUE #1

The taxpayers request the Department to rule on the application of sales/use tax to the acquisition of tools and subsequent sale of same by parent to the subsidiary.

IC 6-2.5-5-8(b) states:

Transactions involving tangible personal property other than a new motor vehicle are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of the person's business without changing the form of the property.

In the instant case, it is clear both the acquisition of tools by the Supplier (parent) and the subsequent sale of same to the Distributor (subsidiary) fall within the “resale” exemption afforded by above IC 6-2.5-5-8, therefore, these transactions are not subject to sales/use tax.

RULING – ISSUE #1

The Department rules the Supplier's (parent's) acquisition of tools from third-party suppliers and tools machined by a subsidiary of the Supplier on behalf of the Supplier, the Supplier's inspection, etching, and packaging of the tools, and the Supplier's sale of tools to the Distributor (subsidiary) are not subject to Indiana sales/use tax.

DISCUSSION – ISSUE #2

The taxpayers request the Department to rule on the application of sales/use tax to the purchase of tools from the parent by the subsidiary.

The “resale” exemption (IC 6-2.5-5-8; see Discussion - Issue #1) is applicable to the purchase of tools from the Supplier (parent) by the Distributor (subsidiary) in instances where the Distributor sells the tools to customers or sales representatives. In instances where the Distributor supplies tools to the customers or sales representatives located in Indiana at no charge, the Distributor is subject to Indiana use tax on same pursuant to IC 6-2.5-3-2 (imposition statute for use tax). In instances where the Distributor supplies tools to customers or sales representatives located outside of Indiana, the Distributor is not subject to Indiana sales and use tax on such tools, but might be subject to use tax in the state to where the tools are shipped.

RULING – ISSUE #2

The Department rules the purchase of tools from the Supplier (parent) by the Distributor (subsidiary) is not subject to sales/use tax when the Distributor sells the tools to customers or sales representatives. In cases where the Distributor supplies tools at no charge and ships them to customers or sales representatives located in Indiana, the Distributor is subject to Indiana use tax on the tools. In cases where the Distributor supplies tools at no charge and ships them to customers or sales representatives located outside of Indiana, the Distributor is not subject to

Indiana sales and use tax on the tools, but might be subject to use tax in the state to where the tools are shipped.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford taxpayer any protection. It should be noted that subsequent to the publication of this ruling, a change in statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

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